FIN621 Final Term Subjective

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Question No: 49 (Marks: 3)

If a company uses Rs.20, 000 to buy merchandise for inventory. What do you think would be the effect on working capital? Give reason.

If company purchase inventory on cash current assets of company increase and on the other hand cash is decrease. So there is no effect in working capital.

Question No: 50 (Marks: 3)

Ahmad Incorporation has Owner's Equity of amount Rs.75, 000 as an opening balance. During the period, three major transactions occurred:
Issuance of stock: Rs.22, 000
Dividend distribution: Rs.10, 000
Net Loss: Rs.6, 000.

Based on these transactions, what would be the Ahmad's ending balance of Owner's Equity?

Answer

Owner's Equity (beg)	**75000**
Add; Stocks Issued	**22000**
Less; Dividend distribution	**10000**
Less; Net Loss	**6000**
Owner's Equity (end)	**81000**

Question No: 51 (Marks: 5)

ABC Company is famous for its automobiles. The business has undergone the following changes in the month of March. Prepare the journal entries for the transactions.

1. Mar. 1 Owner deposited Rs. 50,000 cash in a bank account in the name of the business.

2. Mar. 5 Purchased land for Rs. 160,000, of which Rs. 40,000 was paid in cash. A short-term note payable was issued for the balance of Rs. 120,000

3. Mar. 6 An arrangement was made with the XYZ Company to provide parking privileges for its customers. XYZ Company agreed to pay Rs. 1,200 monthly, payable in advance. Cash was collected for the month of March.

4. Mar. 7 Arranges with Times Printing Company for a regular advertisement in the Times at a monthly cost of Rs. 390. Paid for advertisement during March by check, Rs. 390

5. Mar. 15 Parking receipts for the first half of the month were Rs. 1,836, exclusive of the monthly fee from XYZ Company

1. bank 50,000
cash 50,000

2. land 160,000
cash 40,000
notes payable 120,000

3. Cash 1200
Unearned parking revenue 1200

4. Advertisement cost 390
bank 390

5. cash 636
Unearned parking revenue 1200
Parking revenue 1836

Question No: 52 (Marks: 5)

Following data is taken from the ABC Corporation.

	1999 (Rs.)	2000 (Rs.)
Total assets	400,000	300,000
Total liabilities	300,000	180,000
Share capital (Rs. 10 par	100,000	90,000
Total debt	120,000	140,000

Requirement:
Calculate the following.
a) Debt ratio (2.5)
b) Debt to total asset ratio (2.5)

Debt ratio = total debt / total assets
= 120000/ 400000
= .3
Debt ratio = total debt / total assets
= 140,000/300,000

= .46

Debt to total assets ratio = total debt / total assets
= 120000/400000
= .3
Debt to total assets ratio = total debt / total assets
= 140000/300000
= .46

Question No: 53 (Marks: 5)

Assume that you wish to invest in the stocks of a high-tech corporation and that one of your investments goals is to receive dividend income from the stocks that you purchase. You begin your research by examining Microsoft, one of the world's most successful software corporations. You quickly discover that, as of 1997, Microsoft had never paid a dividend. Furthermore, the company's 1997 balance sheet reported holdings of nearly Rs. 9 billion in cash and highly liquid securities. With all of these liquid resources available, why do you suppose that Microsoft has never paid a cash dividend to its stockholders?

As the cash balance as well as liquid securities of the company are on high side which depicts that the company has never paid cash dividend but paid stock dividend instead of cash dividend. if the company had paid cash dividend , its cash balance and liquid securities would have been reduced.

Paper#2

Question No: 43 (Marks: 3)
If the retained earnings account has a debit balance, how is it presented in the balance sheet and what is it called?
If a corporation has experienced significant net losses since it was formed, it could have negative retained earnings (reported as a debit balance instead of the normal credit balance in its Retained Earnings account). When this is the case, the account is described as "Deficit" or "Accumulated Deficit" on the corporation's balance sheet.

Question No: 44 (Marks: 3)
Using the following information, compute the dividend yield to the nearest tenth.
Income Rs. 130,000
Beginning shares outstanding 250,000
Ending shares outstanding 270,000
Current price per share Rs. 7.50
Dividend per share Rs. 1.20

Dividend yield = divi per share / market price
= 1.20/7.50
= 0.16

Question No: 45 (Marks: 3)

What information is provided by the balance sheet to the short term and log term creditors?

short-term creditors: Interest of short-term creditors is to watch the ability of business to meet its debts as these become due; i.e. Short-term solvency. They want to see whether business has the ability to meet its current liabilities out of its current assets. If the entity can not maintain a short-term debt paying ability, it will not be able to maintain a long-term debt-paying ability, nor will it be able to satisfy its stockholders.

long-term creditors: Interest of long-term creditors is to see the long-term solvency of the business and rate of return on their loans. Solvency is the ability to meet outside liabilities from total assets. Indicators of solvency are the **Long-term Solvency,** which are as follows:-

i) **Debt –To-Total-Assets:** The debt-to-total assets ratio is derived by dividing a firm's

total debt by its total assets: It indicates percentage of total assets financed by debt

= Total outside liabilities /Debt = 75 = 37.5%

Total assets (total liabilities +shareholders funds) 200

Question No: 46 (Marks: 5)

Assume that you are a commercial loan officer at a large bank. One of your clients recently submitted an application for Rs. 300,000 five year loan. You have worked with this business before on numerous occasions and have periodically been forced to deal with late and missed payments attributed to cash flow problems. Thus you are surprised to see in the business plan accompanying the application that the management expects to reduce the company s operating cycle from 190 days to 90 days. A footnote to the business plan indicates that the reduction in the operating cycle will result from a tighter credit policy and the implementation of a just-in-time inventory system.

Requirement:

Would the company be able to reduce the operating cycle by applying the new strategy and would you give the loan to the company on this basis?

As the company has reduced its operating cycle from 190 days to 90 days which has tightened the credit policy, as a result of which sales of the company will be reduced which will decrease the revenue of the company and profit of the company will also be decreased. Implementations of just in time inventory system will also tight the liquid position of the company. Keeping in view this situation, application for loan of Rs. 300,000 will not be exceed to by the bank.

Question No: 47 (Marks: 5)

In each of the following situations, indicate the form of organization that you would expect the business to take.

a) A neighborhood lawn-moving business operated by a teenager

b) A company organized to manufacture an electric car
c) A small retail clothing store, owned and operated by a brother and sister
d) A medical group consisting of six doctors, organized in a state that does not allow professional practices to incorporate.
e) A flight school owned by an airline pilot. The business is profitable, but the owner uses the profits to buy planes and expand the business.

a) **Sole Proprietorship**
b) **Limited company**
c) **Sole proprietorship**
d) **partnership firm**
e) **Sole proprietorship**

paper#3

Question No: 49 (Marks: 3)

What do you understand by the efficiency of the operating cycle?

Efficiency of operating cycle/process: It is determined by activity ratios, keeping in view the conversion process, which is as follows:-

Cash/assets ---- → Inventory ----→ Receivables ---- → Cash
Processing Sales, collection

Operating Cycle=Inventory sale days (average) +Receivable Collection days (average).

The shorter the operating cycle, the higher the quality of current assets and the greater the efficiency of management.

Question No: 50 (Marks: 3)

What will be the effect on the book value per share of the common stock of a company, if the corporation obtains a loan?

When a corporation obtains a bank loan there is no effect upon book value per share of common stock. Assets and liabilities both increase by its amount. Therefore, net assets will remain unchanged.

Question No: 51 (Marks: 5)

Current assets and current liabilities data for companies D and E are summarized as follows:

	Company D	Company E
Current assets	Rs. 400,000	Rs. 900,000
Current liabilities	200,000	700,000
Working capital	Rs. 200,000	Rs. 200,000

Requirement:

Evaluate the relative liquidity of the companies. Which company is more favorable?

- **For Company D:**

  Current Ratio = Current Assets / Current Liabilities

  = 400,000 / 200,000

  = **2**

- **For Company E:**

  Current Ratio = Current Assets / Current Liabilities

  = 900,000 / 700,000

  = **1.285**

Company D is more liquid then E.

Question No: 52 (Marks: 5)

Following is the balance sheet of the ABC Company.

ABC Corporation

Balance Sheet

Mar. 31, 1991

Assets	
Cash	Rs. 12,500
Notes receivables	104,000
Accounts receivables (net)	68,500
Inventories at cost	50,000
Plan & equipment (net of depreciation)	646,000
Total assets	**Rs. 881,000**
Liabilities & Stockholder's equity	
Accounts payable	Rs. 72,000
Notes payable	54,500
Accrued liabilities	6,000
Common stock (60,000 shares, Rs. 10par)	600,000
Retained earnings	148,500
Total liabilities and owner's equity	**Rs. 881,000**

Requirement:

Calculate the current ratio and quick ratio for both years. (2.5+ 2.5)

- **Current Ratio=Current Assets / Current Liabilities**

  = 235,000 / 132,500

  = 1.77

- **Quick Ratio** = Current Assets - Inventories / Current Liabilities

  = (235,000 – 50,000) / 132,500

  = 185,000 / 132,500

  = 1.39

Question No: 53 (Marks: 5)

You have been given the two years data of XYZ company as follows:

	2005	2004
Net sales	1,493,622	1,403,243
Assets:		
Beginning of the year	1,039,731	889,584
End of year	1,1143701	1,039,731

Calculate the Total Assets Turnover ratio for both years.

- **For Year 2005:**

  Total Assets Turnover Ratio = net sales / total assets

  = 1,493,622 / 1, 114, 3701

  = 0.134

- **For Year 2004:**

  Total Assets Turnover Ratio = 1,403,243/ 1,039,731

  = 1.349

Paper#4

Question No: 45 (Marks: 3)

How does working capital help management in making rationale decisions?

Management of working capital

Guided by the above criteria, management will use a combination of policies and techniques for the management of working capital[16]. These policies aim at managing the *current assets* (generally cash and cash equivalents, inventories and debtors) and the short term financing, such that cash flows and returns are acceptable.

- **Cash management. Identify the cash balance which allows for the business to meet day to day expenses, but reduces cash holding costs.**
- **Inventory management. Identify the level of inventory which allows for uninterrupted production but reduces the investment in raw materials - and minimizes reordering costs - and hence increases cash flow; see Supply chain management; Just In Time (JIT); Economic order quantity (EOQ); Economic production quantity (EPQ).**
- **Debtors management. Identify the appropriate credit policy, i.e. credit terms which will attract customers, such that any impact on cash flows and the cash conversion cycle will be offset by increased revenue and hence Return on Capital (or *vice versa*); see Discounts and allowances.**
- **Short term financing. Identify the appropriate source of financing, given the cash conversion cycle: the inventory is ideally financed by credit granted by the supplier; however, it may be necessary to utilize a bank loan (or overdraft), or to "convert debtors to cash" through "factoring".**

Question No: 46 (Marks: 5)

Consider the following information.

Cash Rs. 15,000

Beginning net receivables Rs. 55,000

Ending net receivables Rs. 57,000

Net sales Rs. 640,000

Net credit sales Rs. 480,000

Cost of goods sold Rs. 390,000

Average inventory Rs. 62,000

Requirement:

Compute the receivable turnover to the nearest tenth.

Receivables turn over ratio = Net credit sales /Average Debtors

= 480,000 / [(55,000+57,000)/2]

= 480,000 / 56,000

= 8.57

Question No: 48 (Marks: 5)

Assume that you are a graduate student and going to form a web page consultancy firm. You are very young and compassionate to form this company. You need a bank loan of Rs.50,000 for computer equipment , as a collateral you have a bike your father gave you after securing 80% marks in FSc. Not wanting to lose your bike and to protect yourself you decided to organize a corporation. Explain will it be beneficial idea for you or not.

At the time of giving loan, the bank needs collateral as a security by hypothecation of bike in favour of bank in order to secure its loan in case of default but the physically the bike will remain in use with the graduate student. I will be a beneficial idea to form a wed page consultancy firm.

Question No: 49 (Marks: 10)

The data shown below were taken from the financial records of J Ltd at the end of the year. The financial year of the company ends on 31, December each year.

Accounts Payable	Rs 50,000	Accrued Liabilities	Rs. 33,000
Cash	32,000	Inventories Jan	42,000
Inventories Dec	38,000	Marketable Securities	10,000

Operating Expenses	120,000	Prepaid Expenses	25,000
Purchases (Net)	360,000	Accounts Receivable Jan	61,000
Accounts Receivable Dec	61,000	Long Term Loan	150,000
Plant Assets	400,000	Sales	604,000
Sales Returns	20,000	Retained Earning	133,000
Share Capital (Rs.10 Par) Interest expense	**92,000** 30,000	Market Price	18

On the basis of above information, calculate the following.

a. Debt ratio (4)

b. Debt to equity ratio (2)

c. Debt to total asset ratio (4)

Question No: 50 (Marks: 10)

How many types of audit opinions are there? Assume that you have been appointed as an Auditor of the company, after the audit of the company, what can be your possible audit opinions. Briefly explain each of the audit opinion.

Paper#5

1) differentiate between profit and profitability(3 marks)

Profit is one of financials performances of a company and an evidence of its success, which is achieved if the income exceeds the expenses. Profit growth determines the potential growth of the company, increases its business activity.

The term "profitability" has its origin from the rent, which literally means income. Thus, the term "profitability" in broad sense refers to yield, revenue performance and efficiency.

Profitability indicators are used for comparative assessment of individual businesses performance and industries that produce different amounts and types of products.

2) why retained earnings are more preferable for stockholders than net income?(3 marks)

Retained earnings are more preferable for stockholders because retained earning are part and parcel of equity capital. While calculating the net worth of the business, equity capital + retained earnings + additional paid in capital are add up. Book value per share increases as the retained earnings increases.

Question No: 48 (Marks: 10)
The year end balance sheet of LaserTech, Inc includes the following stockholder s equity section. Stockholder s equity:
Rs. 8 cumulative preferred stock, Rs. 100 par value,
callable at Rs. 103, 200,000 shares authorized
Rs. 6,000,000
Common stock, Rs. 2 par value, 5,000,000 shares
authorized:
Issued Rs.
3,600,000
Subscribed 1,400,000 5,000,000
Additional paid in capital
Preferred Rs. 240,000
Common (including subscribed shares) 25,000,000 25,240,000
Retained earnings 3,690,000
Total stockholder s equity Rs. 39,930,000
Assets of the corporation include subscriptions receivable, Rs. 5,600,000.

Requirement:
a. How many shares of commons stock have been issued or subscribed? (2)
b. What is the total legal capital, including shares subscribed? (2)
c. What is the total paid in capital, including shares subscribed? (3)
d. What is the book value per share of the common stock, assuming that no dividends in arrears. (3)

Question No: 49 (Marks: 10)
Listed below is the working capital information for ABC Company, at the beginning of the year.

Cash Rs. 405,000
Temporary investment in marketable securities 216,000
Notes receivables current 324,000
Accounts receivables 540,000
Allowance for doubtful accounts 27,000
Inventory 432,000
Prepaid expenses 54,000
Notes payable within one year 162,000
Accounts payable 445,000
Accrued liabilities 40,500

The following transactions are completed during the year:
1. Sold on account inventory costing Rs. 72,000 for Rs. 65,000
2. Issued additional shares of capital stock for cash, Rs. 800,000
3. Sold temporary investments, Rs. 60,000, for Rs. 54,000 cash
4. Acquired temporary investments costing Rs. 105,000. paid cash
5. Wrote off uncollectible accounts, Rs. 18,000
6. Sold on account inventory costing Rs. 75,000 for Rs. 90,000
7. Acquired plant and equipment for cash, Rs. 480,000
8. Declared a cash dividend, Rs. 240,000
9. Declared a 10% stock dividend
10. Paid accounts payable, Rs. 120,000
11. Purchased goods on account, Rs. 90,000
12. Collected cash on accounts receivables, Rs. 180,000
13. Borrowed cash from a bank by issuing a short term note, Rs. 250,000

Requirement:

a) Compute the amount of quick assets, current assets, and current liabilities at the beginning of the year shown by the above account balances (2+2+2)

b) Compute the current ratio, and quick ratio. (2+2)